Economic Commentary

TrustINdiana

Market Commentary for **October 2009**

Economy Still Uncertain Despite Growth

On balance, economic data released in September and October further supported the notion that the U.S. economy is pulling out of the biggest downturn since the Great Depression. The advance estimate of Gross Domestic Product (GDP) growth from the Bureau of Economic Analysis showed that the economy grew at a 3.5 percent annualized rate in the third quarter. Growth was largely driven by consumer spending and federal government spending, while increased imports and sluggish state and local government spending had a slightly negative effect. The third quarter figure represents the first period of positive growth since the second quarter of 2008 and the largest gain since the third quarter of 2007. Year-over-year, GDP is still down 2.3 percent.

The official unemployment rate rose to 10.2 percent in October, the highest since 1983 and up from 9.8 percent in September. If underemployed workers and people who have stopped job-searching are included, the figure is 17.5 percent. Job cuts were fairly broad-based, however education and health care jobs increased, as did those of business/professional services. As often noted, employment tends to be a lagging indicator, so despite the positive GDP growth, unemployment will not likely decrease significantly until sometime in 2010.

Consumer confidence fell in October, largely because of current and future labor market outlooks. The Conference Board index of consumer confidence fell 5.7 points to 47.7 from an upwardly revised 53.4 figure in September. The expectations component of the index, which measures consumer attitudes about the future, plunged to 65.7 from 73.7, while current conditions decreased from 23 to 20.7. Similarly, the University of Michigan consumer sentiment index fell to 70.6 in October from 73.5 in September. The decline in this index was also led by its expectations component. Consumer confidence, while still elevated above the historic lows at the beginning of this year, is expected to remain somewhat depressed until there is significant job growth.

Other consumer-related data in this period were also, for the most part, marginally negative but, significantly, there was little volatility in any of the measures. Personal income was flat in September after two consecutive months of modest gains. Spending declined 0.5 percent.

The saving rate increased to 3.3 percent in September from 2.8 percent in August. During the same month, the core personal consumption expenditures (PCE), which excludes food and energy prices and is the Fed's preferred measure of inflation, rose by 0.1 percent, but is still down 0.5 percent on a year-over-year basis. The core Consumer Price Index (CPI) rose 0.2 percent in September. These figures suggest that inflation is still in check in the short term.

Businesses fared relatively well during the past two months. Retail sales (MARTS) declined 1.5 percent in September, but that was less than expected as the popular cash for clunkers program promoted by the federal government wound down. Indeed retail sales excluding autos rose 0.5 percent in the same period. New orders for manufactured durable goods increased 1.0 percent in September after the downwardly revised 2.6 percent decrease in August, while factory orders also rose by 0.9 percent. The Institute Supply of Management's (ISM) manufacturing index, which measures the overall health of the manufacturing sector, rose to 55.7 in October from 52.6 in September. The index is at its highest level since April 2006 and well beyond the threshold of 50, which indicates the sector is expanding.

Existing home sales jumped 9.4 percent in September month-over-month and annualized sales are at its highest since August 2007. The increase was broad-based, with every region of the country experiencing a gain. The median existing house price declined by 8.5 percent year-over-year, however after a year of significantly higher drops, house price depreciation may be slowing. New home sales fell 3.6 percent in August after steadily rising since March 2009.

The Federal Open Market Committee met on November 3 and 4 and, as expected, kept the fed funds target rate between zero and 0.25 percent. In its released statement, the Fed was once again cautiously optimistic, "Although economic activity is likely to remain weak for a time, the Committee anticipates that policy actions to stabilize financial markets and institutions, fiscal and monetary stimulus, and market forces will support a strengthening of economic growth and a gradual return to higher levels of resource utilization in a context of price stability."

Sector Review

U.S. Treasuries: Corporate earnings continued to improve during the third quarter of this year. A healthy amount of upward earnings helped push the Dow Jones Industrial Average past the 10,000 mark in October for the first time in over a year. Investors in Treasuries continued to see impressive supply absorbed by the marketplace. The path of the recovery remains the focus of the market, along with the timing of the unprecedented Central Bank accommodative monetary policy removal. The 10-year note yield increased to a 3.41 percent yield from a 3.30 percent yield the prior month. The two-year note yield edged downward to a 0.91 percent yield from a 0.95 percent yield while the three-month bill saw yields drop to 0.04 percent from 0.11 percent. (Rates and prices maintain an inverse relationship. Prices decrease as yields increase).

Commercial Paper: Commercial paper supply has stabilized recently although yields remain challenged as the Fed continues to maintain its target rate in the zero to 0.25 percent area. In December, the SEC is expected to announce adjustments to its 2a-7 methodology for money market fund investors. Some combination of stricter weighted average maturities (WAMs) and rating requirements are expected, and much of the industry has positioned its portfolios in anticipation of these potential adjustments. One-month, top-tier, higher quality asset-backed commercial paper (ABCP) names trade between 0.10 percent and 0.40 percent and three-month paper traded between 0.25 percent and 0.75 percent.

U.S. Government Agencies: Agency securities and government backed FDIC paper continue to price at or near levels comparable to where Treasury issues have priced in recent months. The fed funds futures market expects the Fed to continue to be on hold until June 2010 and current pricing levels on the agency curve reflect this belief. Agency yields at month-end on three-month paper yielded near 0.10 percent, six-month paper yielded 0.20 percent, and 12-month paper yielded 0.35 percent.

Strategy: The Federal Reserve continues to maintain its fed funds target range between 0.00 and 0.25 percent. While there are still some signs of reduced pressure on the economy, slow growth remains evident in the remaining quarter of 2009 as the recessionary environment appears to be ebbing and an economic recovery is potentially starting to take hold. In this uniquely challenging environment we continue our focus on being highly defensive by maintaining ample cash and being very selective in identifying approved issuers while implementing trade opportunities to add yield when possible.

DJIA		NASDAQ		S&P 500	
0.004%	10.66%	-3.64%	29.68%	-1.97%	14.71%
Month	Year-to-Date	Month	Year-to-Date	Month	Year-to-Date

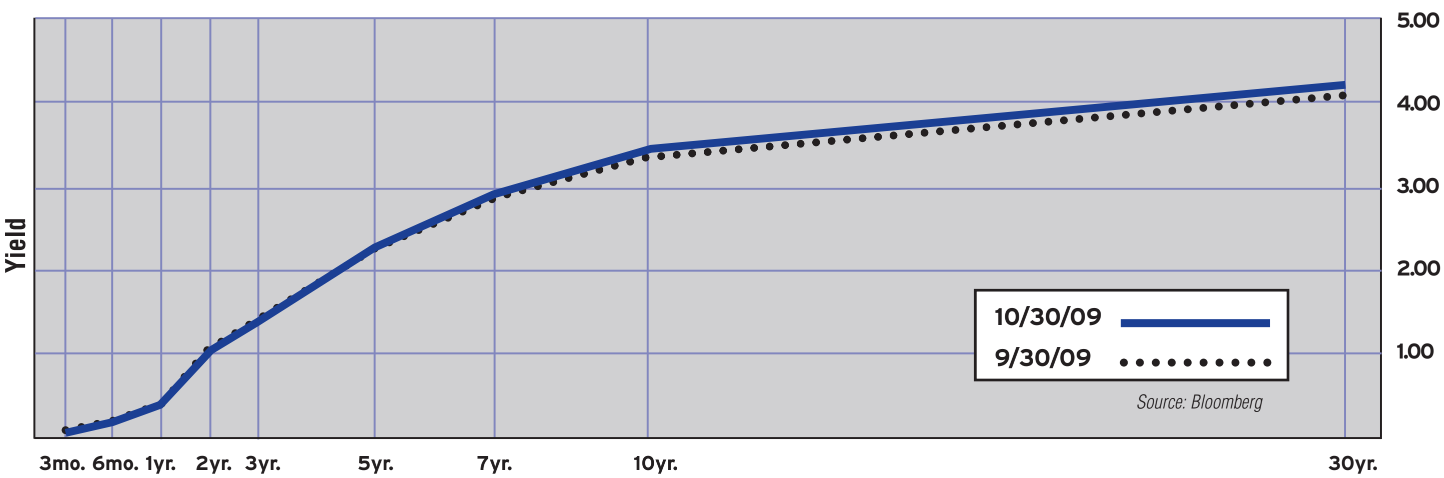
The opinions expressed above are those of TrustINdiana and are subject to change without notice. All statistics represent month-end figures unless otherwise noted.

Market Summary for **October 2009**

Monthly Market Summary - Week-ending Rates and Yields

	10/02	10/09	10/16	10/23	10/30	4th QTR AVG	3rd QTR AVG	2nd QTR AVG	1st QTR AVG
Overnight Rates									
Effective Fed Funds	0.13	0.12	0.12	0.11	0.11	0.12	0.15	0.18	0.18
Repurchase Agreements	0.05	0.00	0.07	0.02	0.05	0.04	0.10	0.14	0.16
Discount Rates									
1 Month Treasury Bill	0.01	0.02	0.05	0.03	0.01	0.02	0.09	0.09	0.10
1 Month Agency Disc.	0.06	0.08	0.09	0.07	0.04	0.07	0.13	0.13	0.17
1 Month Com'l Paper	0.16	0.18	0.15	0.17	0.16	0.16	0.22	0.24	0.36
3 Month Treasury Bill	0.06	0.07	0.07	0.07	0.06	0.07	0.14	0.16	0.18
3 Month Agency Disc.	0.10	0.09	0.11	0.11	0.09	0.10	0.17	0.19	0.30
3 Month Com'l Paper	0.28	0.27	0.23	0.26	0.23	0.25	0.32	0.46	0.71
6 Month Treasury Bill	0.12	0.13	0.13	0.14	0.14	0.13	0.22	0.28	0.33
6 Month Agency Disc.	0.18	0.12	0.17	0.17	0.17	0.16	0.26	0.30	0.47
6 Month Com'l Paper	0.35	0.37	0.31	0.33	0.31	0.33	0.42	0.62	1.04
Yields									
1 Year Treasury	0.37	0.38	0.36	0.40	0.37	0.38	0.45	0.53	0.56
1 Year Agency	0.43	0.43	0.42	0.44	0.42	0.43	0.52	0.73	0.76
2 Year Treasury	0.87	0.96	0.96	1.00	0.89	0.94	1.02	1.02	0.90
2 Year Agency	0.98	1.07	1.07	1.14	1.01	1.05	1.16	1.37	1.60
5 Year Treasury	2.21	2.35	2.35	2.45	2.31	2.33	2.46	2.25	1.77
5 Year Agency	2.60	2.73	2.70	2.80	2.65	2.70	2.87	2.83	2.65

Historical Yield Curve



Key Economic Indicators

	For the Period	Date of Release	Expected	Actual	Prior
Unemployment Rate	October	11/06	9.9%	10.2%	9.8%
Consumer Price Index	September	10/15	-1.4%	-1.3%	-1.5%
- Less Food and Energy	September	10/15	1.4%	1.5%	1.4%
Consumer Conf. (CB)	October	10/27	53.5	47.7	53.1
FOMC Rate Decision		09/23	0%-0.25%	0%-0.25%	0%-0.25%
Gross Domestic Product	3QA	10/29	3.2%	3.5%	-0.7%

TrustINdiana
Office of the Treasurer of Indiana
242 State House, 200 W Washington St.
Indianapolis, IN 46204
www.trustindiana.in.gov